**TESTIMONY OF DAVID W. DANJCZEK**
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**BEFORE THE**
**COMMITTEE ON COMMERCE, SCIENCE AND TRANSPORTATION**
**UNITED STATES SENATE**
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Mr. Chairman, members of the Subcommittee, I appreciate the opportunity to testify before you today. I am the Staff Vice President of UNOVA , Inc. UNOVA is the largest producer of machine tools and manufacturing systems in the United States, with total sales of $2 billion and machine tool sales in excess of $1 billion. Today I appear before you on behalf of AMT-The Association for Manufacturing Technology and will focus my testimony on The United States Government's technology policy and on the issue of how our nation's export controls affect the machine tool industry, particularly those controls as they apply to China.

There seems to be widespread agreement regarding United States export control policies aimed at keeping dangerous technology out of the hands of the so-called pariahs, or rogue states, and AMT strongly supports this policy. Nevertheless, the most difficult issues revolve around what to do about China.

Certainly China presents a dilemma for U.S. export policy. On the one hand, China is a major trading partner and needs to import capital goods, including machine tools, to support its commercial economic development. On the other hand, China is quite clearly viewed by U.S. export licensing authorities as a potential military threat and technology transfer risk.

The picture is no clearer with our allies. There is no consensus within the Western alliance about how to treat technology transfer to China, and there is presently no effective multilateral forum in which to address U.S. Government concerns about dual-use exports. This dilemma has led to the worst of all worlds for both the U.S. Government and U.S. machine tool companies. The Chinese can readily obtain the machine tools they desire, and U.S. companies are denied participation in the business.

UNOVA, particularly our Cincinnati Machine Division, has been a major exporter to China, and so I would like to add something of our own experiences as a U.S. Government licensee. In the days of CoCom, the multilateral organization that coordinated technology transfer during the Cold War, the licensing process was slow and the outcome was uncertain. But we were confident that it provided a level playing field among our potential competitors, with rules that were reasonably clear. Its successor regime, the Wassenaar Arrangement, which has been in existence since 1996, leaves licensing decisions and methods up to individual countries, based on a concept called "national discretion." This arrangement provides neither a level playing field nor clear rules, and our experience operating under it suggests that since CoCom ended, U.S. licensing policies and practices have been far more restrictive than those of our European allies.

As a result of our trade association -- AMT's -- role as a machine tool list technical advisor to the Wassenaar negotiating team, we have conducted studies of the licensing process and its outcomes among Wassenaar members. These studies show that the licensing process in the U.S. is far lengthier and far less certain in outcome than the equivalent process in European countries and Japan. The length of the process and the uncertainty of the outcome combine to put U.S. companies at a tremendous competitive disadvantage in China, even when we are competing for obviously legitimate commercial projects.

In some cases, U.S machine tool manufacturers, including Cincinnati Machine, have been denied even the opportunity to bid on projects in China because of the wariness of the Chinese customer about the likely outcome of the U.S. licensing process. More recently, Chinese customers have asked that my company provide a guarantee that an export license will be obtained as a condition of the order with significant financial penalties to accrue if the license is denied. Of course, no U.S. machine tool company could offer such a guarantee.

The view of these Chinese companies is well justified. Statistics indicate that the United States Government is far more likely to disapprove machine tool licenses for China than any of our European allies. While a mere handful of U.S. machine tool licenses have been approved over the past five years (a total of 25 licenses, or an average of five licenses per year during the period from 1992 through 1997), trade statistics indicate that our European allies have, during that period, shipped a substantial volume of highly sophisticated machine tools to Chinese end-users.

This is reflected in the average unit prices of machine tools exported from Europe to China, which are up to five times the average unit price of machine tools exported from the U.S. to China. Since the technical sophistication, accuracy, and productivity of a machine tool is directly proportional to its selling price, this indicates that the Europeans are shipping to China precisely those machine tools that are likely to be subject to export controls. Trade figures further indicate that by freely selling the same sophisticated machine tools to the Chinese which would be most likely unavailable from United States manufacturers, German, and other European providers, are also garnering sales in the non-controlled machine tool categories, putting U.S. manufacturers at a further disadvantage. Germany alone now has twice the market share of machine tool sales to China as does the United States. This is in marked contrast to the situation in South Korea where favorable export policies by the U.S. Government have led to a 20 percent market share by U.S. companies, twice the market share that we have in China. Of course, exports to Korea have deteriorated sharply due to the Asian financial crisis.

In the past three years, representatives of my company have visited many of the Chinese companies involved in the manufacture of components for commercial aircraft. We were astounded at the number of state-of-the-art European machine tools (all of which required export licenses) that had been delivered into those companies since 1994. Just last week, as John Logan has noted in his testimony, those same European manufacturers were exhibiting their five-axis machines at the China International Machine Tool ("CIMT") show, in Beijing, and assuring their Chinese customers that there would be no problem obtaining an export license from their Governments. Even more significantly, at least seven different Chinese machine tool builders were exhibiting sophisticated machine tools at the show, machines that would require an export license if sold by a U.S. manufacturer as a consequence of features on the Chinese machines such as five axes and very high levels of precision. One Chinese-made spherical lathe had a stated accuracy down to +/- .2 microns, as good as any machine made in the United States, Europe, or Japan. Under a separate cover, I am submitting data and brochures from the CIMT for the record.

Our current multilateral export licensing system certainly isn't keeping the Chinese from acquiring highly sophisticated machine tool technology, since they can readily obtain it from the Europeans or, as the CIMT demonstrated, even manufacture such machines themselves.

By far the most frustrating aspect of this situation is that many of the commercial aircraft factories in China contain joint ventures and co-production arrangements with American aircraft companies.  Some of our industry's most valued domestic customers are moving production work from the U.S. to China to satisfy offset requirements related to Chinese aircraft purchases.  Offsets are the practice by which China (or any other buyer of defense products or machinery) demands that a certain percentage of large capital goods sales to their country be built in their country, or that a comparable amount of business be directed to China as an "offset" for the large capital goods contracts that China signs.

China already accounts for seven percent of Boeing Company's sales. Boeing projects that China will become the largest aircraft market outside of the U.S. and could, within seven years, account for nearly 25 percent of Boeing's total business.  Thus, there is every reason to believe that production of commercial aircraft parts in Chinese factories will continue to grow in tandem with the Chinese demand for commercial aircraft.

The Chinese factories producing parts for American aircraft are often supervised or monitored on site by American managers, yet current U.S. Government export control policy virtually assures that the machine tools used in those factories will be of European, not American, origin.  I am at a loss to understand how this policy enhances our national security.

In sum, as my industry has testified previously, there is a fundamental problem with the current export regime.  Not only does it lack discipline internationally with regard to a country about which the United States Government has indicated technology transfer concerns; it also puts U.S. companies on an uneven playing field with regard to sales to what is likely to be the fastest growing and largest market for capital goods over the coming decade. Repeatedly over the past five years, the United States Government has taken a negative approach toward machine tool sales to China while our allies have not. The result has been that the Chinese have been denied nothing in terms of high technology, but U.S. firms have lost out in a crucial market. This serves neither our commercial nor our strategic interests and needs to be addressed in whatever legislation that is produced during the 106th Congress.

With this as background, I would now like to comment on specific provisions in the Export Administration Act which has just been reported to the Senate by Chairman Phil Gramm's Banking Committee.

First, I would like to commend the Banking Committee for undertaking the critically important task of revising the Export Administration Act ("EAA"). As everyone is aware, the EAA was last amended in 1988, a year before the collapse of the Soviet Union, and the authority of the Act lapsed almost five years ago. Certainly, there is ample justification to draft and adopt a new EAA to guide export controls in the 21st Century. The Banking Committee bill is a strong beginning toward new export control legislation. AMT would like to comment on a few areas where we feel the bill deals with issues important to the machine tool industry.

In earlier testimony, AMT strongly recommended that any export control legislation have a very strong provision defining "foreign availability" in order to reflect the reality in which U.S. companies compete today. Current law defines "foreign availability" as any item that can be supplied from outside the multilateral export control system in sufficient quantity and comparable quality so as to make the existing export controls on any particular item ineffective in achieving the objective of the controls.

Today, however, we operate in a context of weak to non-existent multilateral controls and, as I have pointed out, a multilateral system that allows any member country to use its own "national discretion" to decide whether or not, or how rigorously, to license a product. We agree with the Banking Committee that the new EAA should not be allowed to perpetuate the fiction that the current multilateral export control system functions effectively to deny technology to targets of the multilateral regime, particularly China, which has, at best, an ambiguous status in relation to the Wassenaar Arrangement's list of restricted technologies.

We are pleased that the legislation acknowledges that "foreign availability" can exist *within a multilateral control system, not just outside* that system. We strongly support language in the bill that explicitly acknowledges that “foreign availability" can come from U.S. allies and fellow participants in multilateral export control regimes, such as Wassenaar. The Banking Committee bill mandates that the Secretary of Commerce shall determine that an item has foreign availability status if the item "is available to controlled countries from sources outside the United States, including countries that participate with the United States in multilateral export control regimes." This provision should create a more reasonable "foreign availability" definition, one that reflects the new reality, where "foreign availability" of a controlled product is most likely to come from a U.S. ally rather than a company outside the multilateral control regime.

Nevertheless, We are concerned with the length of time proposed for negotiations to eliminate "foreign availability." In an age when the product cycle for some high technology products is scarcely two years, eighteen months is simply too long a time limit for such negotiations. Either the country in question is willing to stop selling the particular product or technology to the target country, or it is not. For many U.S. companies, a year and one-half would give foreign competitors too great a head start in developing a new market. Thus, in practice, the liberal time limit in the proposed legislation could fatally undermine the stated purpose of the foreign availability provision, which would be to give U.S. companies a fair opportunity to compete for business in products already available to the target country. AMT recommends that the time limit be reduced to six months, or, at most, nine months to ensure a better balance between adequate time for negotiations and competitive consequences to U.S. companies.

Finally, we would recommend that, within the next year or so, the Administration go back to the negotiating table and make a serious effort to strengthen the overall Wassenaar Arrangement. As I have noted, and as the Cox Committee points out, Wassenaar provides weak guidance and almost no discipline upon its members. It is almost worse than having no multilateral regime at all, because it gives the appearance of restricting technology transfer, while leaving all the key judgments up to Wassenaar's constituent members.

Revisions of the Wassenaar charter ought to include far better rules for information exchange than exist today. Under current rules, there is not even a "no undercut" pledge, under which each member state promises not to grant licenses to companies in target countries which have been previously denied licenses by another member of the multilateral regime. At the very least, the U.S. Government ought to be informed beforehand of the intent of other members to grant such licenses, and, at best, there ought to be a commitment among regime members to honor one another's denials.

It is imperative that the status of China be clarified for regime members. If China is not a target of Wassenaar, what is it? Are there any limits on what technology Wassenaar members, at their own discretion, can export to China?

These are the sorts of questions that need to be addressed. They are left ambiguous in the current multilateral arrangement.

The U.S. machine tool industry is highly successful in world markets. Its technology is second to none, and its companies can compete head-to-head and win against the best machine tool companies that Europe and Asia have to offer. But those companies cannot prevail on an uneven playing field. I join my colleagues in urging you to pass an eighteen-year statute of repose during the 106th Congress. I strongly believe that such a law would be a beginning point in the battle to level the playing field with our foreign competitors. I would also like to say a word about the Advanced Technology Program ("ATP") of the Commerce Department. UNOVA has had a very positive experience with the ATP program. Although the vast majority of the funds have gone to the universities that were our partners in this program, we found that the ATP program offers just the right incentive to stimulate cooperative ventures in the new technologies that are necessary to keep American manufacturing ahead of the worldwide competition.

But let me return to the thrust of my testimony. As I have argued, the manner in which the current multilateral export regime is administered by the U.S. Government constitutes a major impediment to accessing key world markets, such as China. I have attempted to detail some of those problems here today. There is some reason for optimism. In particular, we are encouraged by the legislation that has just been reported by the Banking Committee, and it is our hope that an appropriately amended Export Administration bill will become law. We need to create both a domestic and an international regulatory climate that puts U.S. companies on equal footing with their foreign competitors. Our nation's economic health and national security demand no less.

We urge you to support the Banking Committee's EAA renewal when it comes to the Senate floor and to oppose amendments that would make U.S. export control policy even more unilateral than it is today.